

Message Text

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ACTION ARA-10

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B) BOGOTA 8375

C) BOGOTA 8431

D) BOGOTA 8491

E) BOGOTA 8493

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G) BOGOTA 8868

1) ALTHOUGH THE 45-DAY ECONOMIC EMERGENCY DECLARED BY THE LOPEZ ADMINISTRATION IS ONLY HALF OVER AND SEVERAL ADDITIONAL MEASURES REMAIN PENDING, THE EMBASSY BELIEVES THAT A PRELIMINARY EVALUATION, ALBIET WITH MANY UNCERTAINTIES, CAN NOW BE OFFERED. WE WOULD FIRST NOTE THAT NEW MEASURES ISSUED UNDER EMERGENCY DECREE POWERS INCLUDE A NUMBER WHICH EMBASSY AND OTHER OUTSIDE OBSERVERS SUCH AS WORLD BANK AND IMF HAVE FELT WERE NECESSARY FOR SOME TIME. KEY FEATURES OF ALL NEW MEASURES HAV BEEN MODERATION AND ADHERENCE TO CLASSIC ECONOMIC THEORY. SALES AND INCOME TAXES IN PARTICULAR ARE TEXT BOOK MODELS. IN BRIEF THREE-
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WEEK SPAN GOC HAS MADE SWEEPING CHANGES IN FISCAL AND MONETARY

SYSTEM WHICH SHOULD SERVE TO HELP CONTROL INFLATION, REDUCE DEFICIT FINANCING, AND REDISTRIBUTE TAX BURDEN AWAY FROM LOWER-INCOME GROUPS TO LARGE CAPITAL.

2) THE MOST IMPORTANT OF THE NEW MEASURES, REPORTED BY PREVIOUS CABLE, HAVE BEEN THE NEW INCOME AND SALES TAX LAWS, THE REDUCTION OF THE EXPORT TAX CREDIT (CAT), THE ELIMINATION OF THE WHEAT SUBSIDY, AND THE ALTERNATION OF NATURAL GAS POLICY. ADDITIONAL DECREES HAVE REGULATED THE FISCAL OPERATIONS OF DECENTRALIZED GOVERNMENT AGENCIES AND REGIONAL GOVERNMENTS. THE ONLY MAJOR MEASURES STILL EXPECTED ARE A REVISION OF PETROLEUM PRICE POLICY AND SOME FORM OF REGULATION ON WAGES AND PRICES PLUS AN IMPLEMENTING REGULATION TO COMPLEMENT THE INCOME TAX LAW.

3.) OBSERVERS BOTH INSIDE AND OUTSIDE THE ECONOMY EXPRESS CONCERN THAT

THE TOTAL IMPACT MAY BE TO COOL OFF THE ECONOMY TOO MUCH AND, IN CONJUNCTION WITH THE INTERNATIONAL ECONOMIC SITUATION, LEAD TO RECESSION, PRODUCTION COSTS ARE RISING AS A RESULT OF INCREASED COSTS OF IMPORTS AND LABOR SLAES, PARTICULARLY FOR ITEMS CLASSIFIED AS LUXURIES SUCH AS AUTOMOBILES AND MAJOR APPLIANCES, ARE EXPECTED TO DECLINE; CREDIT IS EXTREMELY TIGHT AS A RESULT OF NEW MONETARY REGULATIONS; SOME LOSS OF DYNAMISM IS EXPECTED IN THE CONSTRUCTION SECTOR AND EXPORT RECEIPTS WILL PROBABLY SHOW REDUCED GROWTH AS A RESULT OF BOTH REDUCTION OF TAX INCENTIVES AND POSSIBLE SLACKENING OF SOME COMMODITY PRICES. COST OF LIVING INDICES MAY, AS SUGGESTED BY THE NEW ADMINISTRATION, SHOW A SHARP RISE IN THE FOURTH QUARTER AS A RESULT OF ADJUSTMENTS TO THE ECONOMY. THERE HAS ALSO BEEN AN APPARENT INCREASE IN OUTFLOW OF FLIGHT CAPITAL AND THE BLACK MARKET EXCHANGE RATE HAS RISEN SHARPLY TO ABOUT 12 PERCENT OVER OFFICIAL RATE.

4) THE KEY QUESTION WILL BE HOW THE BUSINESS COMMUNITY REACTS WITH RESPECT TO NEW INVESTMENT. IF PRIVATE SECOTR INVESTMENT CONTINUES TO BE STRONG THE ECONOMY SHOULD BE ABLE TO MAINTAIN AN ACCEPTABLE GROWTH RATE OF 5.5-6.0 PERCENT, ALTHOUGH LOWER THAN THE 7 PERCENT RATE OF THE PAST TWO YEARS. AT THE PRESENT TIME MOST OF THE PRIVATE LIMITED OFFICIAL USE

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SECTOR APPEARS TO BE POSTPONING DECISIONS UNTIL A CLEARER READING IS AVAILABLE ON THE IMPACT OF THE NEW MEASURES. ALTHOUGH LITTLE DATA IS AVAILABLE, THERE IS ALSO A CONSENSUS THAT THE ECONOMY HAD ALREADY BEGUN TO SLOW DOWN IN THE THIRD QUARTER IN EXPECTATION OF NEW POLICIES.

5) LARGE INDUSTRIAL FIRMS, WHICH ACCOUNT FOR ABOUT 70 PERCENT OF TOTAL MANUFACTURES, HAVE NOT BEEN GIVEN AN ADDITIONAL TAX BURDEN. WHILE LABOR COSTS WILL PROBABLY

INCREASE AND SALES MAY SUFFER IN SOME AREAS, PROBABLY THE MAJOR FACTOR AFFECTING GROWTH WILL BE UNAVAILABILITY OF CREDIT AND NEW INVESTMENT CAPITAL. COLOMBIAN PRIVATE SECTOR HAS LONG COMPLAINED THAT IT HAS DIFFICULTY IN COMPETING FOR NEW INVESTMENT FUNDS WITH TAX-EXEMPT FINANCIAL INSTRUMENTS. THIS COMPLAINT WILL PROBABLY CONTINUE SINCE EVEN THROUGH TAX/EXEMPTIONS HAVE BEEN REDUCED, INTEREST RATES FOR DEVELOPMENT BONDS WILL BE INCREASED AND EXTENSIVE OPEN-MARKET TREASURY OPERATIONS INITIATED. THE STOCK MARKET DROPPED SHARPLY FOLLOWING ANNOUNCEMENT OF OPEN-MARKET OPERATIONS. AT THE SAME TIME, THEIR PRESENT COMPETITIVE POSITION IS NO WORSE, AND PROBABLY SLIGHTLY BETTER GIVEN THE LOSS OF ATTRACTIVENESS IN SAVINGS AND LOAN DEPOSITS, THAN IN THE PAST TWO YEARS WHEN NEW INVESTMENT AND INDUSTRIAL GROWTH SHOWED SUBSTANTIAL GAINS.

6) GOC OFFICIALS AND FINANCIAL SOURCES, WHILE ACKNOWLEDGING AN UNUSALLY TIGHT CREDIT SITUATION, EXPRESS THE HOPE THAT THIS CONDITION WILL HAVE BEEN LARGELY ALLEVIATED BY THE BEGINNING OF 1975. CONSTRUCTION COULD SHOW REDUCED GROWTH RATES AS A RESULT OF REDUCTION IN INCENTIVES FOR CONSTANT-VALUE SAVINGS AND LOAN DEPOSITS, BUT SOME OF THIS SLACK (AND GREATER EMPHASIS ON LOWER-CLASS HOUSING), MAY BE TAKEN UP BY GOVERNMENT PROGRAMS. CONSIDERABLE DYNAMISM IS EXPECTED IN EXTRACTIVE INDUSTRIES AS A RESULT OF DECISIONS CLEARING THE WAY FOR DEVELOPMENT OF NICKEL AND GAS DEPOSITS (ALTHOUGH THE LAG TIME FOR INITIATING PRODUCTION WILL BE ALMOST FOUR YEARS). MORE ACTIVITY IS ALSO POSSIBLE FOR COAL AND PETROLEUM IF PROBLEMS IN THESE AREAS ARE RESOLVED. NEW PROGRAMS FOR STIMULATING AGRICULTURAL PRODUCTION ARE EXPECTED TO BE ANNOUNCED IN THE NEAR FUTURE AND LIMITS ON REDISCOUNTS FOR AGRICULTURE CREDIT HAVE ALREADY BEEN REMOVED. THE REDUCTION IN EXPORT TAX CREDITS IS BEING LIMITED OFFICIAL USE

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PARTIALLY COMPENSATED FOR THROUGH ACCELERATED DEVALUATION.

7) DESPITE PESSIMISM AND VALID CONCERN BEING SOUNDED IN SOME QUARTERS, EMBASSY'S PRELIMINARY EVALUATION IS THAT COLOMBIAN ECONOMY OFFERS REASONABLE PROSPECTS FOR CONTINUED GROWTH-BUT PROBABLY AT A LOWER RATE IN 1975 THAN DURING PAST TWO YEARS. ALTHOUGH TASK OF REDUCING INFLATION WITHOUT OVERLY AFFECTING GROWTH IS DIFFICULT FOR ANY COUNTRY, QUALIFICATIONS OF PROJECT ADMINISTRATION OFFICIALS AND BASIC STRENGTH IN ECONOMY ARE STRONG POSITIVE FACTORS. FURTHERMORE, SUBSTANTIAL FISCAL AND MONETARY REFORM WAS CLEARLY REQUIRED WERE AN EVEN WORSE SITUATION RESULTING FROM INFLATION TO BE AVERTED. ACCORDINGLY, ALTHOUGH A COMPLETE JUDGEMENT MUST AWAIT FURTHER EVENTS, THE LOPEZ ADMINISTRATION MERITS HIGH MARKS FOR ITS ECONOMIC POLICIES

THUS FAR.

8) OVERALL, THE REACTION TO THE EMERGENCY MEASURES HAS BEEN TO ACCEPT THEM AS NECESSARY, PARTICULARLY IN PRINCIPLE. THERE HAS, HOWEVER, BEEN SOME CRITICISM EXPRESSED BY POLITICIANS AND DOUBTS AND UNCERTAINTY EXPRESSED BY MANY BUSINESSMEN. FORMER PRESIDENT CARLOS LLERAS IN THE INITIAL ISSUE OF HIS PERIODICAL "NUEVA FRONTERA" HAS CRITICIZED THE LOPEZ ADMINISTRATION SEVERELY AND DESCRIBED AS A DANGEROUS PRECEDENT THE USE OF EMERGENCY POWERS TO ACHIEVE FISCAL REFORMS. OTHER CRITICISM HAS BEEN EXPRESSED BY BUSINESSMEN WHO FEEL THAT THE NEW REGULATIONS ARE UNDULY STRICT, AND BY THE DEMOCRATIC LABOR ORGANIZATIONS WHICH HAVE EXPRESSED RESERVATIONS OVER THE EFFECTS THE DECREES WILL HAVE ON WORKERS PURCHASING POWER.

9) LLERAS STRONG CRITICISM OF THE LOPEZ MEASURES WILL PROVIDE A FOCAL POINT FOR FURTHER OPPOSITION TO THE LOPEZ PROGRAM. AT PRESENT, HOWEVER, THE PRESIDENTS SUPPORT, IN THE CONGRESS AND THE PRESS STILL REMAINS QUITE STRONG. BARRING AN UNEXPECTED NEGATIVE RULING FROM THE SUPREME COURT, HE SHOULD BE ABLE TO IMPLEMENT HIS PACKAGE OF ECONOMIC REFORMS WITH THE ADVANTAGE AS OF NOW OF GENERAL PUBLIC SUPPORT.

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